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UNCLAS SECTION 01 OF 03 GUATEMALA 002511

SIPDIS

DEPT PASS USTR FOR FARARZ SIDDIQI
DEPT PASS MILLENNIUM CHALLENGE CORPORATION FOR JIM VERMILLION
AND FRAN MCHAUGHT
TREASURY FOR JAMIE FRANCO
DEPT PASS TO USAID
USAID FOR STEPHEN BRENT

AIDAC

SENSITIVE

E.O. 12958: N/A

TAGS: [EAID](#) [ECON](#) [SOCI](#) [ETRD](#) [PGOV](#) [PREL](#) [KCOR](#) [GT](#) [MCC](#)

SUBJECT: Guatemala and the MCC

[11.](#) (SBU) Summary: Going by MCC statistical procedures, Guatemala is unlikely to be selected to negotiate an MCC compact in FY 2006. But Guatemala's suitability for a compact should be evaluated in a more basic sense: is the Berger administration making progress toward MCC goals, and how do Guatemala's results in the MCC categories compare to similar countries such as Nicaragua and Honduras. Using these criteria Guatemala comes out well. It is important that we recognize the success the Berger administration has achieved in time to have some impact on the developing campaign for the November 2007 presidential elections. With reconstruction and CAFTA implementation looming, now is the time to begin negotiations for an MCC compact with Guatemala. End summary

[12.](#) (SBU) For FY 2006, Guatemala was placed in the Lower-Middle Income Country category for MCC eligibility, where it does not yet meet most Ruling Justly and Investing in People indicators. But stepping back from the statistical exercises there is a strong case to be made for selecting Guatemala for an MCC compact. Under President Berger Guatemala has made important progress in each of the three MCC categories.

DRAMATIC TURN AROUND ON CORRUPTION AND PROGRESS ON RULE OF LAW

[13.](#) (SBU) In the Ruling Justly category, President Berger has engineered one of the more dramatic turnarounds in Latin America. While Portillo and his top officials pilfered state coffers, Berger has gone to war against corruption. He has passed legislation against money laundering and terrorist financing, and has prosecuted, fired or jailed officials from the previous administration, from the Vice President, Finance Minister, Tax Director and Comptroller, to 48 top police officials and 500 officers. His administration has developed a proposal for a new Civil Service Code, signed off on a Freedom of Information Decree for the Executive Branch, and undertaken institutional assessments to improve transparency and internal controls. In addition, his government has outsourced issuing of drivers permits and passports, instituted a public web-site for government procurement, started publishing its budget on the internet, and implemented an Integrated Financial Management System to control public resources.

POLITICAL RIGHTS AND CIVIL LIBERTIES

[14.](#) (SBU) Guatemala has a good record on Political Rights and Civil Liberties, with its citizens enjoying free and fair elections and unhindered freedom of expression. The political opposition is free to organize and criticize, and does so. Under the Berger administration, there have been no political killings, disappearances or arrests, nor have there been restrictions on civil liberties. The 2004 Human Rights Report correctly concluded that the "Government of Guatemala generally respected the human rights of its citizens." Berger's team has done an admirable job in reaching out to Guatemala's marginalized indigenous population, inviting prominent indigenous leaders, including Nobel laureate Rigoberta Mench, to join his administration. Despite the many problems which still need to be addressed, if the latest qualitative data on the Berger -- and not the Portillo -- administration were used for the Ruling Justly indicators, then Guatemala would likely qualify in four of the six categories.

HEALTH AND EDUCATION PROGRESS AND COMMITMENTS

[15.](#) (SBU) In its strategic plans, from the economic program "Vamos Guatemala" to the ten-year "Competitiveness Agenda," the government firmly commits to socio-economic programs very similar to MCC goals. This has already resulted in positive trends in education completion and immunization rates (now about 90%). Overall expenditures on education for FY 2006 will reach 2.5% of GDP, with education and health receiving the largest line item increases in the budget.

DATA SKEWED BY TAX TO GDP RATIO AND NATIONAL INCOME ACCOUNTING

16. (SBU) The Investing in People indicators are low in part because Guatemala has one of the lowest tax to GDP ratios in the world (10.1%). This also skews the percentage of GDP devoted to education and health. However, in 2006, the GOG's 50 year-old baseline for national accounts will be updated to the year 2001, which the IMF expects will result in a downward revision of official GDP by 15%. For MCC statistical purposes this will raise the percentage of GDP spent on education and health. In addition, a new tax bill, better enforcement, and CAFTA inspired economic growth should increase government revenues and social spending in the medium term. The GDP revision could also drop Guatemala from the Lower-Middle Income category.

PROVIDE FUNDING NOW IN ANTICIPATION OF ELECTIONS

17. (SBU) With further follow-through by Berger on his programs, Guatemala could meet MCC criteria as a Lower Middle income country by FY 2007 (if it stays in this category after GDP is revised downward). However, we need to move more quickly. Average Guatemalans, outraged by corruption under Portillo, elected Berger for his honesty and integrity, while the private sector championed his pro-business policies. Negotiation of an MCC contract in the next year would bolster his image with voters during the campaign for the 2007 elections, and facilitate the election of a like-minded candidate -- not necessarily someone from the Berger coalition, but someone who would support government reform and economic liberalization. Guatemala, with its large impoverished indigenous community, remains vulnerable to populist inroads, either home grown or inspired by Chavez and his allies. Supporting the Berger administration now would help keep the populists at bay and avoid the kind of political problems Venezuela, Nicaragua, Bolivia and Ecuador have faced.

NATURAL DISASTER MAKES FUNDING MORE URGENT

18. (SBU) Guatemala has just suffered its worst natural disaster since the 1976 earthquake. Hurricane Stan affected about 30% of the population of 13 million, leaving at least 700 dead, over 1,000 missing, and dozens of bridges and roads destroyed. Estimates have put the damage between \$2-3 billion, equivalent to around 10% of GDP. The storm was a tremendous blow to recent progress in the GOG's development plan, including ambitious efforts to turn-around the long-stagnant rural economy. Reconstruction depends largely on donor assistance and may take years.

GUATEMALA SHOULD NOT BE THE ONLY COUNTRY LEFT OUT

19. (SBU) Guatemala has the lowest per capita US aid level in the region. It receives only a third of what Nicaragua does and half or less than half of what the other Central American countries do, in spite of having worse social indicators. Nicaragua and Honduras have already negotiated MCC compacts and El Salvador is a strong candidate for FY 06. Omission of Guatemala would be widely noted here. Moreover, it does not make political or economic sense to ignore Central America's largest economy and most populous country at a time when we are trying to implement CAFTA and pull the entire region firmly into the camp of good governance and equitable, sustainable economic development. In fact, if "importance to the US" were made an MCC criteria, then surely the poorer Central American countries, with pressing socio-economic problems that directly affect the US through increased migration and trans-national crime should deserve special attention. As Secretary Rice and USTR Portman stated in their letter to Senator Bingaman, "CAFTA strengthens these countries' ability to receive MCC funds, because CAFTA reinforces the statutory criteria for funding under the MCC law."

GUATEMALA SHOULD BE COMPARED TO LOW-INCOME COUNTRIES

10. (SBU) While Guatemala is on the way to meeting MCA criteria as a Lower Middle-Income country, we believe that its placement in this group does not reflect economic and statistical reality. Guatemala is far from meeting the MCC assumption that lower middle income countries are close to "graduating" from foreign aid, since they have private capital flows and relatively high savings and tax rates to combat poverty. There is little long-term credit in Guatemala, the savings rate is minimal, and the tax to GDP ratio is one of the lowest in the world. Guatemala has far more in common with its "poorer" neighbors, Nicaragua and Honduras, and should be compared to them and not to Lower Middle-Income countries such as Brazil and Bulgaria.

11. (SBU) Looking at the median ratings for the Low Income group and considering the qualitative improvements engineered by the Berger administration since January 2004, as well as the upcoming revision of GDP figures, Guatemala would be above the median in all indicators except possibly Rule of Law and Health and Primary Education expenditures. Moreover, even

here, the Berger Administration's commitments and overall positive trends should be given substantial weight. For example, Guatemala's Transparency International rating for 2005 improved 13% over 2004, and is only 0.1 points below those of Nicaragua and Honduras. If Guatemala's excellent record on Economic Freedom and macroeconomic stability is taken into consideration -- which is far above that of other Low Income countries -- it would be a top MCC candidate in the Low Income group.

12. (SBU) In sum, setting the standards for MCC assistance through a process that does not adequately take into account Guatemala's economic reality and the progress made towards meeting MCC criteria does not serve our regional political and economic goals. We have a unique chance to support a government now that is making a sincere and successful effort to tackle inherited socio-economic problems and inequality.

Derham